

CONTRACTING ACTIVITIES

To better serve you, the Arizona Department of Revenue now offers online assistance and filing of your business taxes. To file your taxes online or to register to use the website, go to www.aztaxes.gov

This publication is for general information about Arizona transaction privilege tax on contracting activities. The Arizona transaction privilege tax is commonly referred to as a sales tax. However, the tax is on the privilege of doing business in Arizona and is not a true sales tax. For complete details, refer to the Arizona Revised Statutes and the Arizona Administrative Code. In case of inconsistency or omission in this publication, the language of the Arizona Revised Statutes and the Arizona Administrative Code will prevail.

While reading this brochure, please be aware that the definitions of certain terms, such as “Owner-builder” and “Sub-contractor”, are different under the Arizona Revised Statutes than those commonly accepted within the industry.

Who Must Pay

Prime contractors are subject to transaction privilege tax under the prime contracting classification. A prime contractor is a person who performs, coordinates or supervises construction work, including contracting with any subcontractors. The prime contractor is the person responsible for the completion of the contract.

A prime contractor who only furnishes labor in the performance of contracting work is subject to the tax as well as one who furnishes both labor and materials.

Examples of taxable contracting activities include:

- Construction or demolition of a building
- Road construction
- Construction for government agencies (Federal, state and local), schools, churches, or non-profit organizations (such as hospitals)
- Installation of permanently attached equipment
- Sales and installation of floor covering, including carpeting
- Home remodeling (painting, wiring, plumbing, repairs, etc.)
- Sale of a new manufactured building by a licensed dealer
- Land excavation
- Landscaping

All contractors are considered to be prime contractors and must have a transaction privilege tax license. This includes general contractors, subcontractors and specialty contractors.

What is the Tax Base for Prime Contractors?

The tax base for the prime contracting classification is 65% of the gross proceeds of sales or gross income derived from the job.

What is the Tax Rate, and How Do I Pay?

The current combined state and county tax rates for contracting activities can be found in the *Arizona State, County and City Transaction Privilege and Other Tax Rate Tables* under Business Class Code 015. Most Arizona cities participate in the state collection program and those taxes are reported and paid on the Transaction, Privilege, Use and Severance Tax Return (TPT-1). Most of the larger cities license and collect privilege tax independently of the state. If you are unsure whether your city collects its own tax or if the state collects for it, check the *Arizona State, County and City Transaction Privilege and Other Tax Rate Tables*.

NOTE: *State and county rates are combined for ease of reporting. City taxes are reported separately. See the Form TPT-1 for details.*

Factoring Transaction Privilege Tax

When a business “factors” transaction privilege tax, it means the tax is included in the total price rather than shown as a separate charge. If you choose to factor the tax, the tax must be calculated using a factoring formula. There are many different factoring formulas depending on city taxes, county taxes or differences in allowable city tax deductions. See Arizona Transaction Privilege Tax Procedure TPP 00-1 for information about factoring.

Nontaxable Subcontractors

The determination of whether a contractor is a taxable prime contractor or a nontaxable subcontractor depends on the facts surrounding each individual project. An individual contractor can be a taxable prime contractor on one job and a nontaxable subcontractor on the next job.

In order to be a nontaxable subcontractor on an individual project or job, the following factors must be present:

- a. The job is in the control of a prime contractor who supervises, performs or coordinates the construction work and is responsible for the completion of the contract;
- b. The prime contractor receives gross receipts attributable to the job;
- c. The prime contractor is subject to tax on the gross receipts attributable to the job; and
- d. The prime contractor pays the subcontractor out of the taxable gross receipts attributable to the job
- e. The contractor is given a Prime Contractor’s Certificate (ADOR Form 5005).

Are Materials Taxed?

The retail tax does not apply to the sale of materials to a taxable prime contractor or a subcontractor if the materials become a permanent part of the construction. The retail or rental tax does apply to construction machinery and equipment sold or leased to the contractor for use on a construction job, or any other item that is not incorporated into the project. The retail

CONTRACTING ACTIVITIES

tax also applies to materials purchased directly by an owner-builder.

How Do Contractors Report Transaction Privilege Tax?

Contractors may elect to report and pay taxes based on either the “cash receipts” or “accrual” method when applying for their transaction privilege tax license. A contractor who elects the cash method reports and pays the tax for the month in which cash payments are actually received. A contractor who elects the accrual method reports and pays the tax for the month in which the income is accrued, without regard to when payment is received.

Application of County Taxes

Prime contractors may not have to pay county taxes on income from contracts entered into before the effective date of a county tax, if a contract does not provide that the contractor is entitled to recover the amount of the tax from a purchaser. Such contracts must be pre-qualified and pre-approved by the Department of Revenue.

What Deductions are Allowed?

Prime contractors are:

1. Allowed a deduction for the sales price of land, if it is part of the project, before determining the taxable base. The deduction may not be more than the sales price of the land, not to exceed fair market value.
2. Allowed a deduction for sales and installation of certain groundwater measuring devices.
3. Allowed a deduction for the gross income attributable to the purchase of certain equipment that qualifies for exemption under the retail classification.
4. Allowed a deduction for proceeds from a contract to provide and install a solar energy device. The deduction may not exceed five thousand dollars for each contract.

Bonding Requirements

If you are a new or out-of-state contractor, you must submit a bond to cover your future tax liabilities before you can be issued a transaction privilege tax license. For more information on bonding, please see Pub 539, Taxpayer Bonds brochure.

For Additional Information, call:

Phoenix (602) 255-2060
Toll free from area codes 520 & 928 (800) 843-7196

For Hearing Impaired - TDD only:

Phoenix (602) 542-4021
Toll free from area codes 520 & 928 (800) 397-0256

Or Write to:

Arizona Department of Revenue
Taxpayer Information & Assistance
PO Box 29086
Phoenix AZ 85038-9086

For Related Tax Information:

Internet Address www.azdor.gov
Recorded tax information (602) 542-1991
Toll free from area codes 520 & 928 (800) 845-8192
Forms by Mail (602) 542-4260
Forms by Fax (602) 542-3756

For additional contracting information contact:

Arizona Registrar of Contractors
www.azroc.gov
Phoenix (602) 542-1525
Toll free in Arizona (877) 271-9286
Hearing Impaired TDD line (602) 542-1588

This publication is available in an alternative format upon request.